

Editor's note: 81 LD. 457; Appealed – stipulated dismissal, sub nom. Atlantic Richfield v. Morton, Civ.No. 74-181 (D.Wyo. Nov. 12, 1975); also Appealed – set aside and remanded, sub nom. Marathon Oil Co. v. Kleppe, Civ. No. C74-180 (D. Wyo. Dec. 11, 1975), 407 F.Supp. 1301, aff'd, No. 76-1230 (10th Cir. June 7, 1977), 556 F.2d 982

ATLANTIC RICHFIELD COMPANY
MARATHON OIL COMPANY

IBLA 72-136

IBLA 73-77 Decided August 14, 1974

Appeals from separate decisions of the Director, United States Geological Survey, requiring corrected reports and recalculation of royalties from variable rate royalty leases committed to the Elk Basin (GS-49) and Lost Soldier (GS-44) oil and gas unit agreements.

Affirmed.

Oil and Gas Leases: Unit and Cooperative Agreements

Both the Lost Soldier and Elk Basin unit agreements require the Regional Supervisor for the Geological Survey to exclude input wells located outside the participating area of each unit from the well count he

makes as part of his determination of the variable rate royalty for these unit agreements.

Oil and Gas Leases: Unit and Cooperative Agreements

The Elk Basin and Lost Soldier unit agreements require the unit operator to locate input wells at optimal locations for recovery of the unitized substances anywhere in the unit area, regardless of royalty considerations.

Contracts: Performance and Default: Waiver and Estoppel –Federal Employees and

Officers: Authority to Bind Government – Oil and Gas Leases: Unit and

Cooperative Agreements

Normally, there can be no estoppel against the government based on the incorrect or unauthorized acts of its employees.

APPEARANCES: H. Blair Klein, Esq., Attorney, Marathon Oil Company; Frank B. Friedman, Esq., Attorney, Legal Division, Atlantic Richfield Co.; David C. Branand, Esq., Office of the Solicitor, United States Department of the Interior.

OPINION BY ADMINISTRATIVE JUDGE THOMPSON

These appeals require us to determine if input wells 1/ located outside the participating area, but inside the unitized area of two federal oil and gas unit agreements can be counted as producing wells for royalty purposes. The leases committed to these unit agreements are subject to a variable rate royalty based on the average production per well: as the production increases or the number of wells decrease, the percentage royalty increases.

Atlantic Richfield is the operator of the Lost Soldier unit agreement, and the holder of federal leases Cheyenne 029630(a), 029630(b), 063724, 065546, 065920, and 070341 committed to that unit agreement. Marathon is the holder of two leases, Billings 039112 and Wyoming 05717, which are committed to the Elk Basin unit agreement. We will refer to these parties collectively as "appellants."

The Lost Soldier unit includes the Tensleep oil and gas reservoir. In 1961, an engineering study submitted to the Department showed that the use of water injection to maintain the pressure in the field would increase the recovery in the Tensleep reservoir from 38 percent to 53 percent. As a result of this study, the

1/ A well through which fluid or gas is introduced to increase the pressure in an oil field. They are also known as "repressuring" or "injection" wells.

Lost Soldier unit agreement was drafted and executed. In a unit agreement, owners of working, royalty and other oil and gas interests agree to collectively develop and operate an oil and gas pool, field or like area for the purpose of conserving these resources. One of the lessees is designated as the unit operator. He is responsible for the production and development of the unit. Those portions of the unit which are reasonably proved to be productive of the unitized substances are designated as "participating areas." Each tract placed in a participating area receives a percentage of all unitized substances produced from the area. Sections 1-3, 8, 11 and 13 Lost Soldier Unit Agreement; Mineral Leasing Act of February 25, 1920, 41 Stat. 437, as amended, 30 U.S.C. § 181 et seq. (1970).

Atlantic Richfield counted input wells located outside the Tensleep participating area but inside the Lost Soldier unit area as producing wells. Until March 25, 1970, royalty payments calculated on that basis were accepted, without comment, by the United States Geological Survey (Survey). On that date, the Regional Petroleum accountant sent Atlantic Richfield a letter advising that the counting of input wells within the unit, but outside the Tensleep participating area was not a proper basis for calculating royalties. The Acting Regional Oil and Gas Supervisor confirmed the Regional Accountant's determination in a decision dated September 29, 1970.

His decision was, in turn, affirmed by the Acting Director of the Survey on September 16, 1971. Atlantic Richfield appealed this decision to the Board.

The Elk Basin unit includes the Embar-Tensleep participating area. In 1967, a peripheral waterflooding program was begun to increase the recovery in this area. As in the case of the Lost Soldier unit discussed above, input wells were initially counted as producing wells even though they were outside the participating area of the unit. On November 3, 1971, the Acting Oil and Gas Supervisor for the Northern Rocky Mountain Region decided that this practice was improper. The Acting Director for the Survey affirmed this decision on July 11, 1972. Marathon now appeals this decision.

In both cases, the Acting Director's rationale for his decision was identical. In the decision on the Lost Soldier unit he said:

Inasmuch as the Lost Soldier unit agreement specified that for purposes of computation of royalty rates the "average production shall be determined in accordance with the operating regulations as though each participating area were a single consolidated lease" and since the oil and gas operating regulations limit the well count for determining royalties due on step-scale and sliding-scale leases to "wells on the leasehold", it is clear that the Supervisor is without authority to permit the inclusion of injection wells located outside the governing participating area in the well count used to determine the royalty rate due the United States on production allocated to any Federal leases on which the royalty rate depends on the daily average production per well.

We are considering these appeals together because they present the identical issue for review. Royalties for the leases committed to each unit agreement are determined by reference to the operating regulations and separate but essentially identical provisions of the unit agreements. Both the Elk Basin and Lost Soldier unit agreements provide that royalties for leases with variable rate royalties are to be computed by: (1) treating the participating area of each unit agreement as if it were a single consolidated lease; and (2) by reference to the operating regulations, in this case, 30 CFR 221.49.

Appellants argue, in essence: (1) the only rational interpretation of the operating regulation, 30 CFR 221.49, is that it is specifically designed to authorize inclusion of input wells in the well count for royalty computation of variable rate leases whether or not such wells are located inside or outside of a unit participating area; (2) the Survey's decision is contrary to the "clear purpose and plain meaning of the regulation," or if the regulation is ambiguous, it must be construed against the Government; (3) the Government is estopped because of its long administrative practice to the contrary to change the regulation; 2/ and (4) subparagraph (b) of 30 CFR 221.49 should be a separate part of the regulation.

2/ The administrative practice involved is approval of input wells in development plans and acceptance of royalties. Approval in a development plan is a prerequisite to drilling wells and is made

Appellants' first assertion is that the only rational interpretation of 30 CFR 221.49 is that it is specifically designed to include all input wells in the well count for royalty purposes. The regulation is organized into one main paragraph and nine subparagraphs. The main paragraph prescribes the general mechanism for computing the variable royalty rate for unit agreements. The nine subparagraphs prescribe rules for particular aspects of royalty rate calculation.

The regulation, 30 CFR 221.49, minus the irrelevant subparagraphs, states:

[1] Sliding- and step-scale royalties are based on the average daily production per well. The supervisor shall specify which wells on a leasehold are commercially productive, including in that category all wells, whether produced or not, for which the annual value of permissible production would be greater than the estimated reasonable annual lifting cost, but only wells which yield a commercial volume of production during at least part of the month shall be considered in ascertaining the average daily production per well. [2] The average daily production per well for a lease is computed on the basis of a 28-, 29-, 30-, or 31-day month (as the case may be), the number of wells on the leasehold counted as producing and the gross production from the leasehold. (Tables for computing royalty on

(fn. 2 cont.)

independently of any royalty consideration. The approval concerns only the geological and engineering aspects of the operating plan, and cannot be construed to affect the proper determination of the royalty. The effect of the acceptance of the royalties is discussed infra.

the sliding-scale and on the step-scale basis may be obtained upon application to the supervisor.) [3]
The supervisor will determine which commercially productive wells shall be considered each month as producing wells for the purpose of computing royalty in accordance with the following rules, and in his discretion may count as producing any commercially productive well shut-in for conservation purposes:

* * * * *

(b) Wells approved by the supervisor as input wells shall be counted as producing wells for the entire month if so used 15 days or more during the month and shall be disregarded if so used less than 15 days during the month.

[Emphasis and bracketed numbers added.]

According to the unit agreements, each participating area is to be treated as a consolidated lease. The term "on the leasehold," in the regulations, therefore refers to the participating area of the unit only. Section 14 Lost Soldier Unit Agreement; Section 21 Elk Basin Unit Agreement.

The sentence numbered [1] sets forth the basis for royalty computation: average daily production per well. The sentences numbered [2] and [3] and the subparagraphs direct the Supervisor how to determine average daily production per well. The sentence numbered [2] prescribes the time period over which production is to be averaged (a 28-, 29-, 30-, or 31-day month); where the wells to be counted must be located (on the leasehold); and where the oil produced must come from (the leasehold). Again, the term "on the

leasehold" refers only to the participating area of the unit. The sentence numbered [3] directs the Supervisor to refer to nine subparagraphs to determine for the month in question which wells on the leasehold have been used in a manner that qualifies them to be counted as producing wells. Subparagraph (b) tells the Supervisor that for input wells, the minimum prerequisite period of use is 15 days. The organization of the regulation compels us to conclude, contrary to appellant's assertions, that the location limitation in the sentence numbered [2] in the main paragraph applies to all of the subparagraphs. The regulation has been in the present form since 1942. 7 F.R. 4137 (1942). There is no logical reason to place the provision concerning input wells where it is if the qualifications of the main paragraph do not apply to it. The regulation is not specifically designed to include input wells in the well count.

We also find that there is no reasonable basis to the assertion that the regulation is ambiguous and we decline to construe it against the Government. Tri-Cor, Inc. v. United States, 458 F.2d 113, 126 (Ct. Cl. 1972); Standard Oil Co. v. Morton, 450 F.2d 493, 494 (9th Cir. 1971). We conclude that the requirements in the sentence numbered [2] of 30 CFR 221.49 apply to all nine subparagraphs, including subparagraph (b). The Supervisor for the Lost Soldier and Elk Basin unit agreements has no authority to include input

wells located outside the participating area of each unit in the well count made as a part of his determination of the variable rate royalty for these unit agreements.

Appellants assert that the purpose of the unit agreement is to promote conservation by maximizing recovery of unitized substances and that construing 30 CFR 221.49 to exclude certain input wells from the royalty computation is counter to that purpose. Regulations, like statutes, must be construed consistently with the purpose of enactment. Rucker v. Wabash Railroad Co., 418 F.2d 146, 149 (7th Cir. 1969). The purpose of oil and gas unit agreements approved by the government is not only promotion of conservation, but also maximization of revenue for the Government. Standard Oil v. Hickel, 317 F. Supp. 1192, 1195 (D. Alas. 1970), aff'd, 450 F.2d 493 (9th Cir. 1971). See California Co. v. Udall, 296 F.2d 384, 388 (D.C. Cir. 1961). Marathon states:

The obvious reason for authorizing injection wells to be counted as producing wells under the regulations for royalty computation purposes is to encourage the use of such wells to promote the conservation of oil and gas resources and to maximize the recovery thereof without waste.

This argument fails to recognize that both unit agreements, in sections captioned "Conservation," 3/ require the operator to

3/ Section 23 Elk Basin unit agreement and section 16 Lost Soldier unit agreement.

use the most economical and efficient recovery methods to achieve maximum economic yield of the unitized substances. This conservation requirement is totally independent of the royalty clause. There is no cross reference from royalty to conservation in either the unit agreement or the operating regulations. The unit operator must locate input wells at optimal locations for recovery of the unitized substance anywhere in the unit area regardless of the royalty impact. The location of input wells based only on royalty considerations would violate the terms of the unit agreement if the placement did not coincide with the maximum recovery of unitized substances. Appellants' argument, that excluding input wells not in the participating area from royalty well counts is contrary to the purpose of the agreement, is not credible, since the conservation requirement exists independently of any royalty considerations.

The final argument is that because the Survey accepted lower payments in the past, they are now estopped from pursuing the correct interpretation of the unit agreement and regulations. As we stated in Marathon Oil Co., 16 IBLA 298, 81 I.D. , (1974), also decided today, normally, there can be no estoppel against the government based on the incorrect or unauthorized acts of its employees. E.g., Atlantic Richfield Co. v. Hickel, 432 F.2d 587, 591 (10th Cir. 1970). Our decision in Marathon Oil Co., supra, includes a full discussion of this issue in an almost identical factual context. Based on that decision, we hold there is no estoppel in this case.

We also doubt whether the companies could show the necessary reliance even if this were a situation where estoppel was applicable. In its Supplemental Statement of Reasons to the Acting Director of the Survey, Marathon stated:

We do not contend that the countability of these wells for royalty computation purposes was specifically discussed with representatives of the Survey either by the Appellant or by the operator or that the Regional Supervisor affirmatively promised that these wells would be countable for royalty computation purposes. We do say, as is implicit from the circumstances, that these injection wells were regarded for all purposes by all persons involved as being exactly like any other injection wells located inside of participating areas. The simple fact is that the locations of wells were not regarded as significant for any purpose.

It appears from this statement that Marathon was not relying on any acts by Departmental employees, but on its own mistaken interpretation of the Agreement.

Atlantic Richfield has requested that this Board grant oral argument pursuant to our discretionary authority in 43 CFR 4.25. In Atlantic Richfield's brief, it has presented its reasons for overturning the decision of the Survey. These have been considered. We see no useful purpose for an oral argument, nor would the Board's consideration of the case be facilitated thereby. Therefore, the request for oral argument is denied.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decisions appealed from are affirmed.

Joan B. Thompson
Administrative Judge

We concur:

Martin Ritvo
Administrative Judge

Anne Poindexter Lewis
Administrative Judge

